UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

MINNEAPOLIS FIREFIGHTERS' RELIEF ASSOCIATION, on behalf of itself and all others similarly situated,

Plaintiff,

-against-

AMBAC FINANCIAL GROUP, INC., ROBERT J. GENADER, PHILLIP B. LASSITER, SEAN T. LEONARD and THOMAS J. GANDOLFO,

Defendants.

Case No. 08 CV 1918

JURY TRIAL DEMANDED

CLASS ACTION COMPLAINT

Minneapolis Firefighters' Relief Association, ("Plaintiff"), by its attorneys, individually and on behalf of all others similarly situated, alleges the following based upon the investigation of Plaintiff's counsel, except as to allegations specifically pertaining to Plaintiff, which are based on personal knowledge. The investigation of counsel included, among other things, a review of Ambac Financial Group, Inc.'s ("Ambac or the "Company") public filings with the United States Securities and Exchange Commission (the "SEC"), press releases issued by the Company, public conference calls, media and news reports about the Company, and publicly available trading data relating to the price and volume of Ambac's securities.

NATURE OF THE ACTION

1. This action is a securities fraud class action brought under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 10b-5 promulgated thereunder by the Securities Exchange Commission (the "SEC"). It is brought on behalf of a class consisting of all persons who purchased Ambac's securities between October 19, 2005 and

January 15, 2008, inclusive (the "Class Period"), to recover damages caused to the Class by defendants' violations of the securities laws.

2. Ambac is a New York-based holding company which provides financial guarantee products and financial services to public and private sector clients through its subsidiaries. Ambac Assurance Corporation is purported to be its primary operating subsidiary.

3. One type of financial guarantee product Ambac provides is monoline insurance, which is a guarantee of the timely repayment of bond principal and interest when a bond issuer defaults. By providing the guarantee, Ambac causes the insured bond to receive Ambac's triple-A rating, which reduces the financing costs for the issuer and may dramatically increase the marketability of the bond.

4. Initially, Ambac principally insured municipal bonds, which are typically highly rated even before they are insured and carry a very low likelihood of default. However, in recent years, Ambac has increasingly been insuring riskier, complex structured products such as mortgage-backed securities ("MBS") and collateralized debt obligations ("CDO"), which may contain high risk components, including tranches of subprime MBS. Ambac has also been participating in credit default swaps and investing in CDOs, including CDOs the Company insures, further exposing it to the risk of the underlying assets (i.e., subprime mortgages).

5. During the Class Period, Ambac misrepresented its CDO and subprime market exposures and losses, and disclosed only selective, misleading information about its activities in the CDO market. One way it did this was by failing to mark down its CDO and MBS assets in a timely manner, resulting in materially false and misleading financial statements and press releases. The failure to disclose its involvement in the CDO market not only deceived the public about the health of Ambac, but it also skewed the risk measurement exposures in Ambac's SEC

filings. Thus, during the Class Period, Ambac misrepresented its risk management activities and fraudulently misstated its actual level of risk.

6. The truth regarding Ambac's involvement in and exposure to the CDO market began to leak out in July 2007, when the Company reported certain mark-to-market losses for its credit derivatives portfolio due to CDOs containing significant amounts of subprime residential mortgages as collateral. Subsequently, throughout the remainder of 2007, the Company made additional partial disclosures concerning its involvement in and exposure to CDOs, but these disclosures continued to materially understate Ambac's true CDO exposure.

7. In late 2007, CDOs were subjected to increasing scrutiny by the ratings agencies, and many were downgraded following review.

8. Likewise, Ambac and its CDO holdings began to come under greater scrutiny by the ratings agencies and analysts alike. In December, Fitch Ratings, Inc. ("Fitch") announced its completion of a review of Ambac's CDO and residential mortgage-backed securities portfolio, stating that the Company would be required to increase its capital reserves by $1 billion in order to maintain its triple-A credit rating with the agency.

9. Additionally, Standard & Poor's ("S&P") announced in December 2007 that it was changing its outlook for Ambac from "stable" to "negative," indicating that the Company's triple-A credit rating would be at a heightened risk of being cut in the next two years due to deteriorating mortgage debt.

10. On January 16, 2008, Ambac announced its preliminary fourth quarter 2007 results, which amounted to an estimated net loss of approximately $3.4 billion due to losses in its credit derivatives portfolio. Approximately $1.1 billion of the total $5.4 billion in mark-to-

market losses recognized for the quarter were related to CDOs backed by subprime residential mortgage-backed securities.

11. On the same day, Moody's announced it was putting Ambac's AAA rating on review for possible downgrade.

12. Following these announcements, Ambac's share price hit a new 52-week low of $4.50 on January 17, 2008, and closed at $6.24 per share.

13. Subsequently, on January 18, 2008, Fitch downgraded Ambac from AAA to AA and S&P put Ambac's rating on review for possible downgrade. The Company's stock declined further to close at $6.20 per share.

14. Defendants' false and misleading statements throughout the Class Period caused Ambac's stock to trade at artificially inflated prices, trading as high as $96.08 in May 2007. When the truth about the Company's true financial condition was finally revealed, the share price withered to a mere $6.20 per share.

JURISDICTION AND VENUE

15. The claims asserted arise under §§10(b) and 20(a) of the 1934 Act and Rule 10b-5 promulgated thereunder. Jurisdiction is conferred by §27 of the 1934 Act, and venue is proper pursuant to that provision because Ambac and the Individual Defendants conduct business in this District and the wrongful conduct took place here.

THE PARTIES

16. Plaintiff, Minneapolis Firefighters' Relief Association, purchased Ambac securities as detailed in the attached certification and was damaged thereby.

17. Ambac is a New York-based holding company whose subsidiaries provide financial guarantee products and financial services to both public and private sector clients. Ambac Assurance Corporation is its primary operating subsidiary.

18. Defendant Robert J. Genader ("Genader") is, and at all relevant times was, a director, President and Chief Executive Officer ("CEO") of Ambac, and, since July 2006, has been Chairman of the Board. Genader additionally serves as Chairman, President and CEO of Ambac Assurance. During the Class Period, Genader was responsible for the Company's false financial statements and reaped proceeds of $26.4 million by selling his Ambac stock at artificially inflated prices.

19. Defendant Phillip B. Lassiter ("Lassiter") was, at relevant times, Chairman of the Board and CEO of Ambac from July 1991 until January 2004 and Chairman until his retirement in July 2006. Lassiter remains as a director of the Company. During the Class Period, Lassiter was responsible for the Company's false financial statements and reaped proceeds of $40.5 million by selling his Ambac stock at artificially inflated prices.

20. Defendant Sean T. Leonard ("Leonard") is, and at all relevant times was, Senior Vice President and Chief Financial Officer "("CFO") of Ambac and Ambac Assurance. During the Class Period, Leonard was responsible for the Company's false financial statements.

21. Defendant Thomas J. Gandolfo ("Gandolfo") is, and at all relevant times was, Senior Managing Director of Ambac and Ambac Assurance. Gandolfo also serves as head of Global Structured Credit, Derivative Products, Fixed Income Investment Management and Risk Transfer groups of Ambac. Gandolfo joined Ambac in 1994. During the Class Period, Gandolfo was responsible for the Company's false financial statements and reaped proceeds of nearly $1.9 million by selling his Ambac stock at artificially inflated prices.

22. Genader, Lassiter, Leonard and Gandolfo are collectively referred to herein as the "Individual Defendants". The Individual Defendants and Ambac are collectively referred to herein as "Defendants."

CLASS ACTION ALLEGATIONS

23. Plaintiff brings this action as a class action pursuant to Federal Rules of Civil Procedure 23(a) and 23(b)(3) on behalf of a class of all persons who purchased Ambac securities during the period from October 19, 2005 through January 15, 2008, inclusive (the "Class"). Excluded from the Class are Defendants, the officers and directors of the Company, members of the immediate families of any excluded person, the legal representatives, heirs, successors or assigns of any excluded person, and any entity in which Defendants have or had a controlling interest.

24. The members of the Class are so numerous that joinder of all members is impracticable. While the exact number of Class members is unknown to Plaintiff at the present time and can only be ascertained through appropriate discovery, Plaintiff believes that there are hundreds of members of the Class located throughout the United States. At the commencement of the Class Period, Ambac had approximately 105 million shares of common stock outstanding, which were actively traded on the NASDAQ National Market System in an efficient market.

25. Plaintiff's claims are typical of the claims of the members of the Class. Plaintiff and all members of the Class have sustained damages because of Defendants' unlawful activities alleged herein. Plaintiff has retained counsel competent and experienced in class and securities litigation and intends to pursue this action vigorously. The interests of the Class will be fairly and adequately protected by Plaintiff. Plaintiff has no interests which are contrary to or in conflict with those of the Class that Plaintiff seeks to represent.

26. A class action is superior to all other available methods for the fair and efficient adjudication of this controversy. Plaintiff knows of no difficulty to be encountered in the management of this action that would preclude its maintenance as a class action.

27. Common questions of law and fact exist as to all members of the Class and predominate over any questions solely affecting individual members of the Class. Among the questions of law and fact common to the Class are:

a. whether the federal securities laws were violated by Defendants' acts and omissions as alleged herein;

b. whether Defendants misstated and/or omitted to state material facts in their public statements and filings with the SEC;

c. whether Defendants participated directly or indirectly in the course of conduct complained herein; and

d. whether the members of the Class have sustained damages and the proper measure of such damages.

AMBAC'S FALSE & MISLEADING STATEMENTS

28. The Class Period begins on October 19, 2005, when Ambac issued a press release announcing its third quarter 2005 results, which stated in relevant part:

> Ambac Financial Group, Inc. (Ambac) today announced third quarter 2005 net income of $175.1 million, or $1.61 per diluted share. This represents a 5% decrease from third quarter 2004 net income of $183.5 million, and a 2% decrease in net income per diluted share from $1.65 in the third quarter of 2004. The third quarter 2005 results were negatively impacted by a loss provision amounting to $60.0 million on an after-tax basis, or $0.55 per diluted share, related to its exposure to municipal finance credits impacted by Hurricane Katrina.
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> Commenting on the overall results, Ambac President and Chief Executive Officer, Robert J. Genader, noted, "Our operating results,

excluding the $0.55 per share impact of Hurricane Katrina, were pretty good considering the tight credit spreads and increased competition that have persisted during the past 18 months. Domestic top-line production in both public and structured finance was encouraging, with attractive deals closed in a wide array of sectors. European booked business was sparse despite strong activity and growing pipelines - it remains a lumpy and less predictable business flow with long lead times." Mr. Genader continued, "The story of the quarter was Hurricane Katrina and the physical destruction and human suffering that it wrought. While early in the assessment process, we have completed a detailed loss analysis using the best information we could develop. By its very nature, it will be an evolving situation which will require and get our full attention on surveillance and active remediation. ***On a positive note, the balance of our risk portfolio showed improvement.***"

Revenues

Highlights

Credit enhancement production in the third quarter of 2005 was $256.6 million, down 6% from the third quarter of 2004 which came in at $273.7 million. Growth in U.S. public finance was more than offset by a decline in production in U.S. structured finance and international.

Credit enhancement production for the nine months of 2005 of $853.5 million was 10% lower than credit enhancement production of $943.6 million in the same period of 2004 primarily driven by tighter credit spreads across many of the markets that Ambac serves.

Net premiums earned and other credit enhancement fees for the third quarter of 2005 were $231.1 million, which represented an 18% increase from the $195.3 million earned in the third quarter of 2004. Net premiums earned increased for all market sectors but was most significant in U.S. public finance where accelerated premiums were very strong during the quarter.

Net premiums earned include accelerated premiums, which result from refundings, calls and other accelerations recognized during the quarter. Accelerated premiums were $48.9 million in the third quarter of 2005 (which had a net income per diluted share effect of $0.26), up 133% from $21.0 million ($0.11 per diluted share) in accelerated premiums in the third quarter of 2004. The third quarter 2005 was impacted by one large refunded transaction, representing almost half of the total accelerated amount. Long-term interest rates have remained relatively low during 2005 and we continue to see strong refunding activity in our public finance segment. However, as interest rates rise, the level of accelerated premiums should decline.

Net investment income for the third quarter of 2005 was $110.6 million, representing an increase of 22% from $90.5 million in the comparable period of 2004. Net investment income excluding net investment income from Variable Interest Entities ("VIES") for the third quarter of 2005 was $98.5 million, representing an increase of 10% from $89.6 million in the third quarter of 2004. This increase was due primarily to the growth in the investment portfolio driven by ongoing collection of financial guarantee premiums and fees and a net positive adjustment to investment income for certain municipal securities within the investment portfolio that have been pre-refunded. A pre-refunding shortens the maturity of a bond resulting in accelerated amortization of bond premium or discount These positive effects on investment income during the period were partially offset by a lower reinvestment rate and use of cash for repurchases of Ambac stock during 2005 totaling approximately $300 million. Net investment income from VIES for the third quarter of 2005 was $12.1 million, up from $0.9 million in the third quarter of 2004. Investment income from VIES results from the consolidation of certain trusts that Ambac has insured and consolidated under accounting pronouncement FIN 46. The increase in interest income from VIES reflects the consolidation of two transactions executed in the fourth quarter of 2004. Investment income from VIES is offset by interest expense on VIES, shown separately in the Consolidated Statements of Operations.

Net investment income (including net investment income from VIES) for the nine months of 2005 was $317.1 million, representing an increase of 19% from $267.1 million in the comparable period of 2004, primarily as a result of the reasons provided above.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) decreased $3.7 million quarter of 2005 from $86.6 million at June 30, 2005 to $82.9 million at September 30, 2005.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on insured transactions that are considered adversely classified. Ambac continuously monitors its insured portfolio actively seeking to mitigate claims. The ACR increased by $79.3 million during the quarter, primarily as a result of municipal exposures to the region impacted by Hurricane Katrina. Ambac's exposure to losses as a result of the hurricane is derived primarily from its guarantees of municipal bonds in the greater New Orleans area and the Gulffront regions that were most severely impacted by the storm. The company has classified 35 individual obligations in the region with total net par outstanding of approximately $1.1 billion. To date, Ambac has paid three claims on obligations in the region, totaling approximately

$2.0 million and has subsequently recovered the full amounts. In determining our loss estimate, our analysis has considered the unprecedented nature of the disaster, including the displacement of the communities' residents, and the unique aspects of each insured bond, such as the nature of the revenue source, the level of debt service reserves, if any, and other transaction protections. Ambac's estimate of losses related to the hurricane was made without regard to any potential federal, state or local government assistance to individual municipalities or institutions. The credit loss estimation process involves the exercise of considerable judgment. Due to the nature of the loss reserve estimate, Ambac's ultimate actual loss associated with the hurricane may be materially different than the current estimate and thereby may affect future operating results. Ambac will continue to assess the impact of Hurricane Katrina on the fourth quarter and subsequent periods as more information becomes available to us. Ambac does not have material exposure to credits adversely affected by Hurricane Rita. Outside of the ACR activity related to the hurricane, the remaining portfolio experienced slightly favorable credit migration during the quarter.

Other Items

Total net securities gains/(losses) for the third quarter of 2005 were $14.5 million on a pre-tax basis, or $0.08 per diluted share; consisting of net realized gains on investment securities of $9.5 million, net mark-to-market gains on credit and total return derivatives of $3.9 million and net mark-to-market gains on non-trading derivative contracts of $1.1 million. For the third quarter of 2004, net securities gains/(losses) were $10.1 million on a pre-tax basis, or $0.06 per diluted share; consisting of net realized gains on investment securities of $6.6 million, net mark-tomarket gains on credit and total return derivatives of $3.0 million and net mark-tomarket gains on non-trading derivative contracts of $0.5 million.

Total net securities gains/(losses) for the nine months of 2005 were $53.1 million, or $0.27 per diluted share, consisting of net realized gains on investment securities of $10.8 million, net mark-to-market losses on credit and total return derivatives of ($7.0) million and net mark-to-market gains on non-trading derivative contracts of $49.3 million. As discussed in the previous quarter, the mark-to-market gains on non-trading derivative contracts related almost entirely to interest rate hedge contracts related to long-term fixed rate liabilities in Ambac's investment agreement business that were highly effective from an economic perspective but did not meet the technical requirements of FAS 133. As of July 1, 2005, the hedges were redesignated to meet the technical requirements and it is expected that the mark-tomarket of the hedge and hedged item will substantially offset each other in the income statement prospectively. For the nine months of 2004 net securities gains

> were $29.3 million, or $0.17 per diluted share, consisting of net realized gains on investment securities of $27.6 million, mark-to-market gains on credit derivatives and total return swaps of $15.2 million and net mark-to-market losses on non-trading derivative contracts of ($13.5) million.
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> Balance Sheet
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> Highlights
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> Total assets as of September 30, 2005 were $19.06 billion, up 2% from total assets of $18.74 billion at December 31, 2004. The increase was driven by cash generated from business written during the period offset by a decrease in the unrealized gains in the investment portfolio driven by higher long-term interest rates and stock repurchases during the period. As of September 30, 2005, stockholders' equity was $5.19 billion, a 3% increase from year-end 2004 stockholders' equity of $5.02 billion. The increase was primarily the result of net income during the period, offset by lower "Accumulated Other Comprehensive Income," driven by higher long-term interest rates and stock repurchases during the period.

(Emphasis added.)

29. On January 25, 2006, Ambac announced its fourth quarter 2005 financial results in a release entitled, "Ambac Financial Group, Inc. Announces Fourth Quarter Net Income of $204.3 Million, up 8%; Fourth Quarter Net Income Per Diluted Share of $1.90, up 12%." The announcement stated, in part:

> Ambac Financial Group, Inc. (Ambac) today announced fourth quarter 2005 net income of $204.3 million, or $1.90 per diluted share. This represents an 8% increase from fourth quarter 2004 net income of $188.8 million, and a 12% increase in net income per diluted share from $1.69 in the fourth quarter of 2004.
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> Commenting on the overall results, Ambac President and Chief Executive Officer, Robert J. Genader, noted, ***"Our top-line credit enhancement production results are encouraging as we successfully closed a wide array of transactions during the quarter, including a few deals of significant size. Overall, market conditions remain challenging, yet our experienced professionals continue to identify new and attractive opportunities across a broad spectrum of asset classes and geographic locations. I remain cautiously optimistic going into***

2006 as demand for our core financial guaranty product seems to be on the rise."

Revenues

Highlights

Credit enhancement production in the fourth quarter of 2005 was $395.8 million, up 15% from the fourth quarter of 2004 which came in at $344.2 million. Strong growth in U. S. public finance and U. S. structured finance were partially offset by a decline in international.

Credit enhancement production for the full year 2005 of $1,249.4 million was 3% lower than credit enhancement production of $1,287.8 million in 2004, driven by tighter credit spreads across many of the markets Ambac serves and a slow down in transactions in the international market, primarily Europe.

Net premiums earned and other credit enhancement fees for the fourth quarter of 2005 were $217.5 million, which represented a 14% increase from the $190.4 million earned in the fourth quarter of 2004. Increases in net premiums earned in U.S. public finance and U.S. structured finance were partially offset by decreased net premiums earned in international.

Net premiums earned include accelerated premiums, which result from refundings, calls and other accelerations recognized during the quarter. Accelerated premiums were $35.4 million in the fourth quarter of 2005 (which had a net income per diluted share effect of $0.19), up 179% from $12.7 million ($0.07 per diluted share) in accelerated premiums in the fourth quarter of 2004. The majority of the accelerated premiums relate to the U.S. public finance segment. The current quarter was once again impacted by one large public finance refunded transaction, representing 41 % of the total accelerated amount. Long-term interest rates remained relatively low during the year and we experienced extremely high refunding activity in our public finance segment. However, as interest rates rise, the level of accelerated premiums should decline.

Net investment income for the fourth quarter of 2005 was $109.0 million, representing an increase of 16% from $94.0 million in the comparable period of 2004. Net investment income excluding net investment income from Variable Interest Entities ("VIES") for the fourth quarter of 2005 was $96.7 million, representing an increase of 6% from $90.9 million in the fourth quarter of 2004. This increase was due primarily to the growth in the investment portfolio driven by ongoing collection of financial guarantee premiums and fees, partially offset by a

lower reinvestment rate and use of cash for repurchases of Ambac stock during the second and third quarters of 2005 totaling approximately $300 million. Net investment income from VIES for the fourth quarter of 2005 was $12.3 million, up from $3.1 million in the fourth quarter of 2004. Investment income from VIES results from the consolidation of certain trusts that Ambac has insured and consolidated under accounting pronouncement FIN 46. The increase in interest income from VIES reflects the consolidation of two transactions executed in the fourth quarter of 2004. Investment income from VIES is offset by interest expense on VIES, shown separately in the Consolidated Statements of Operations.

Net investment income (including net investment income from VIES) for the full year 2005 was $426.1 million, representing an increase of 18% from $361.1 million in the comparable period of 2004, primarily as a result of the reasons provided above.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) increased $20.2 million during the fourth quarter of 2005 from $82.9 million at September 30, 2005 to $103.1 million at December 31, 2005. The increase was primarily related to a new case reserve established during the quarter for a public finance infrastructure transaction and an addition to an existing case reserve for a stressed health care transaction.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on adversely classified insured transactions. ***Ambac continuously monitors its insured portfolio actively seeking to mitigate claims.*** The ACR decreased by $7.2 million during the quarter, primarily as a result of net improvement in the classified portfolio and a transfer of ACR reserves to case reserves related to the public finance infrastructure transaction discussed above. At December 31, 2005, the specific Hurricane Katrina-related provision amounted to $91.5 million, down slightly from $92.0 million at September 30 due to amortization and pay downs on effected credits. Approximately $1.1 billion of Katrina-impacted credits are included in Ambac's adversely classified credit portfolio. Ambac did not pay any Katrina-related claims during the quarter and has fully recovered the amounts paid in the third quarter. Ambac's estimate of losses related to the hurricane does not consider any potential, federal, state or local government assistance to individual municipalities or institutions as such assistance still has not been determined. The credit loss estimation process involves the exercise of considerable judgment. Ambac will continue to assess the impact of Hurricane Katrina on subsequent periods as more information becomes available to us and the ultimate actual loss

associated with the hurricane may be materially different than the current estimate and thereby may affect future operating results.

Other Items

Total net securities gains/(losses) for the fourth quarter of 2005 were $20.0 million, or $0.12 per diluted share; consisting of net realized losses on investment securities of ($2.2) million, net mark-to-market gains on credit and total return derivatives of $22.0 million and net mark-to-market gains on non-trading derivative contracts of $0.2 million. For the fourth quarter of 2004, net securities gains/(losses) were $16.5 million, or $0.09 per diluted share; consisting of net realized gains on investment securities of $7.5 million, net mark-to-market gains on credit and total return derivatives of $11.9 million and net mark-to-market losses on non-trading derivative contracts of ($2.9) million.

Total net securities gains/(losses) for the full year 2005 were $73.1 million, or $0.40 per diluted share, consisting of net realized gains on investment securities of $8.6 million, net mark-to-market gains on credit and total return derivatives of $15.0 million and net mark-to-market gains on non-trading derivative contracts of $49.5 million. As discussed in the previous quarters, the mark-to-market gains on non-trading derivative contracts related almost entirely to interest rate hedge contracts related to long-term fixed rate liabilities in Ambac's investment agreement business that were highly effective from an economic perspective but did not meet the technical requirements of FAS 133. The hedges have been redesignated to meet the technical requirements and it is expected that the mark-to-market of the hedge and hedged item will substantially offset each other in the income statement prospectively. For the full year 2004 net securities gains were $45.8 million, or $0.27 per diluted share, consisting of net realized gains on investment securities of $35.1 million, net mark-to-market gains on credit and total return derivatives of $27.1 million and net mark-to-market losses on non-trading derivative contracts of ($16.4) million.

Balance Sheet

Highlights

Total assets as of December 31, 2005 were $19.77 billion, up 5% from total assets of $18.75 billion at December 31, 2004. The increase was driven by cash generated from business written during the period and the proceeds of the $400 debt issuance in December 2005 (discussed below), offset by stock repurchases during the period and the decrease in the unrealized gains in the investment portfolio driven by higher long-term interest rates. As of December 31, 2005, stockholders' equity was $5.40 billion, a 7% increase from year-end 2004 stockholders' equity of

$5.02 billion. The increase was primarily the result of net income during the year, offset by stock repurchases and lower "Accumulated Other Comprehensive Income" driven by slightly higher long-term interest rates.

(Emphasis added.)

30. On April 26, 2006, Ambac announced its first quarter 2006 results in a release which stated, in part:

> Ambac Financial Group, Inc. (Ambac) today announced first quarter 2006 net income of $221.1 million, or $2.06 per diluted share. This represents a 19% increase from first quarter 2005 net income of $185.5 million, and a 24% increase in net income per diluted share from $1.66 in the first quarter of 2005.
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> Commenting on the overall results, Ambac President and Chief Executive Officer, Robert J. Genader, noted, "***This was another solid quarter for Ambac in a challenging business environment.*** The company's scale, market diversification and capacity continue to be highly valued by our global clients. These important attributes enable us to participate across a broad spectrum of profitable transactions both domestic and international." Mr. Genader further commented, "Although very large transactions were generally absent during the first quarter, several notable international deals have already closed in April."
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> Revenues
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> Highlights
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> Credit enhancement production in the first quarter of 2006 was $233.5 million, up 17% from the first quarter of 2005 which came in at $199.0 million. Growth in international and U. S. structured finance were partially offset by a decline in U.S. public finance.
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> Net premiums earned and other credit enhancement fees for the first quarter of 2006 were $208.4 million, which represented a 2% decrease from the $211.7 million earned in the first quarter of 2005. Increases in net premiums earned in U. S. public finance and U. S. structured finance were partially offset by decreased net premiums earned in international.
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> Net premiums earned include accelerated premiums, which result from refundings, calls and other accelerations recognized during the quarter. Accelerated premiums were $25.0 million in the first quarter of

2006 (which had a net income per diluted share effect of $0.11), down 28% from $34.5 million ($0.17 per diluted share) in accelerated premiums in the first quarter of 2005. The majority of the accelerated premiums relate to the U.S. public finance segment. As long-term interest rates rise, the level of accelerated premiums from refundings should decline from prior years' levels. Accelerated premiums in the first quarter of 2006 and 2005 include $7.7 million and $4.5 million, respectively, related to the impact of reinsurance cancellations, as discussed below under "Reinsurance Cancellations."

Net investment income for the first quarter of 2006 was $114.0 million, representing an increase of 12% from $102.0 million in the comparable period of 2005. Net investment income excluding net investment income from Variable Interest Entities ("VIES") for the first quarter of 2006 was $101.8 million, representing an increase of 12% from $90.7 million in the first quarter of 2005. This increase was due primarily to the growth in the investment portfolio driven by ongoing collection of financial guarantee premiums and fees and a $200 million capital contribution from the parent company in the fourth quarter of 2005. Net investment income was also modestly affected by increases in interest rates. Net investment income from VIES for the first quarter of 2006 was $12.2 million, up from $11.3 million in the first quarter of 2005. Investment income from VIES results from the consolidation of certain trusts that Ambac has insured and consolidated under accounting pronouncement FIN 46. Investment income from VIES is offset by interest expense on VIES, shown separately in the Consolidated Statements of Operations.

Other income for the first quarter of 2006 was $29.5 million, significantly higher than $2.4 million reported in the comparable period of 2005. During the first quarter of 2006, Ambac sold the remaining three aircraft from a previously reported defaulted enhanced equipment trust certificate transaction. The gain on the sale of the aircraft amounted to $25.0 million and is included in "other income" rather than as a loss recovery because the aircraft had been classified as operating assets for the short period of time in which the company took possession of them after the default.

Financial services. The financial services segment is comprised of the investment agreement business and derivative products business. The investment agreement business is managed with the goal of approximately matching the cash flows of the investment agreement liabilities with the cash flows of the related investment portfolio. The primary activities in the derivative products business are intermediation of interest rate and currency swap transactions and taking total return swap positions on certain fixed income obligations. Gross interest income less gross interest expense from investment and payment agreements plus results from the

derivative products business, excluding net realized investment gains and losses and unrealized gains and losses on total return swaps and non-trading derivative contracts, was $11.7 million in the first quarter of 2006, down 22% from $15.0 million in the first quarter of 2005. The decrease was driven by lower inception revenues on new business in the derivative products business, partially offset by spread improvement in the investment agreement business.

Reinsurance Cancellations

During the first quarter 2006 Ambac cancelled its remaining reinsurance contracts with two reinsurers - AXA Re Finance S.A. and American ReInsurance Company and recaptured $3.9 billion of par outstanding. Both reinsurers had exited the financial guarantee reinsurance business in 2003. Included in ceded premiums in our Consolidated Statement of Operations is $37.0 million in returned premiums from the cancellations, of which approximately $29.3 million was deferred. The difference, $7.7 million, included in accelerated premiums, results from the difference between the negotiated amount of returned premiums and the associated unearned premium remaining on the previously ceded portion of the underlying guarantees....

During the first quarter 2005 Ambac cancelled a reinsurance contract with Radian Reinsurance Inc and recaptured approximately $7.5 billion of par outstanding. Included in ceded premiums in our Consolidated Statement of Operations is $55.8 million in returned premiums from the cancellation, of which approximately $51.3 million was deferred. The difference, $4.5 million, is included in accelerated premiums.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) increased $18.2 million during the first quarter of 2006 from $103.1 million at December 31, 2005 to $121.3 million at March 31, 2006. The increase was primarily related to additional case reserves for a public finance infrastructure transaction and an MBS transaction, partially offset by $7.8 million in payments during the quarter.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on adversely classified insured transactions. Ambac continuously monitors its insured portfolio actively seeking to mitigate claims. The ACR decreased by $25.9 million during the quarter, primarily as a result of net improvements in the classified portfolio and a transfer of ACR reserves to case reserves for the MBS transaction noted above. At March 31, 2006, the specific Hurricane Katrina-related provision amounts to $91.1 million, down slightly from

> $91.5 million at December 31, 2005. Approximately $1.1 billion of Katrina-impacted credits remain in Ambac's adversely classified credit portfolio. Ambac did not pay any Katrina-related claims during the quarter.
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> Other Items
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> Total net securities gains/(losses) for the first quarter of 2006 were $13.5 million, or $0.08 per diluted share; consisting of net realized gains on investment securities of $5.1 million, net mark-to-market gains on credit and total return derivatives of $7.2 million and net mark-to-market gains on non-trading derivative contracts of $1.2 million. For the first quarter of 2005, net securities gains/(losses) were $9.1 million, or $0.05 per diluted share; consisting of net realized gains on investment securities of $1.9 million, net mark-to-market gains on credit and total return derivatives of $6.0 million and net mark-to-market gains on non-trading derivative contracts of $1.2 million.
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> Balance Sheet
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> Highlights
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> Total assets as of March 31, 2006 were $19.74 billion, up 1% from total assets of $19.73 billion at December 31, 2005. The increase was driven by cash generated from operations during the period, partially offset by the decrease in unrealized gains in the investment portfolio driven by higher long-term interest rates and stock repurchases during the period amounting to approximately $30.0 million. As of March 31, 2006, stockholders' equity was $5.47 billion, a 2% increase from year-end 2005 stockholders' equity of $5.37 billion. The increase was primarily the result of net income during the period, offset by stock repurchases and lower "Accumulated Other Comprehensive Income" driven by higher long-term interest rates.

31. On July 26, 2006, Ambac issued a press release entitled, "Ambac Financial Group, Inc. Announces Second Quarter Net Income of $238.6 Million, up 28%; Second Quarter Net Income Per Diluted Share of $2.22, up 31%; Second Quarter Credit Enhancement Production $531.0 Million, up 33%." This release further stated:

> Ambac Financial Group, Inc. (Ambac) today announced second quarter 2006 net income of $238.6 million, or $2.22 per diluted share. This represents a 28% increase from second quarter 2005 net income of $186.1 million, and a 31% increase in net income per diluted share from $1.69 in the second quarter of 2005.

***

Commenting on the overall results, Ambac Chairman and Chief Executive Officer, Robert J. Genader, noted, ***"I am encouraged by the strong credit enhancement production and solid financial results for the quarter. The company's ability to produce record results in this suboptimal business environment is a testament to our people and our strategy. We continue to uncover attractive opportunities to put our capital to work in the short-term and I am confident that the company is well positioned both domestically and internationally for the long-term."***

Revenues

Highlights

Credit enhancement production in the second quarter of 2006 was $531.0 million, up 33% from the second quarter of 2005 which came in at $397.9 million. Growth in international and U. S. structured finance was partially offset by a decline in U.S. public finance.

Credit enhancement production for the six months of 2006 of $764.4 million was 28% higher than credit enhancement production of $596.9 million in the same period of 2005.

Structured finance earned premiums and other credit enhancement fees grew 9%. The rate of growth in structured finance has improved as the recent level of writings in asset classes such as commercial asset-backed securities, auto securitizations and pooled debt obligations has increased. Narrow credit spreads and high prepayment speeds in the mortgage-backed and home equity book of business and early terminations of transactions in other structured finance sectors continue to partially offset the positive effects of new business writings.

International earned premiums and other credit enhancement fees decreased by 6%. The decline was driven primarily by significant paydowns and calls over the past several quarters, a slow-down in new business generated in the past several quarters prior to this quarter, and the recent business mix which has trended towards long-dated infrastructure transactions that earn premiums over a longer period of time than typical structured finance exposures.

Net investment income for the second quarter of 2006 was $117.0 million, representing an increase of 12% from $104.5 million in the comparable period of 2005. Net investment income excluding net investment income from Variable Interest Entities ("VIES") for the second quarter of 2006 was $104.5 million, representing an increase of

13% from $92.2 million in the second quarter of 2005. This increase was due primarily to growth in the investment portfolio driven by the ongoing collection of financial guarantee premiums and fees and a $200 million capital contribution from the parent company in the fourth quarter of 2005. Net investment income was also modestly affected by recent increases in interest rates. Investment income from VIES is offset by interest expense on VIES, shown separately in the Consolidated Statements of Operations.

Financial services revenues were $22.5 million in the first half of 2006, up 24% from the $18.2 million of revenues in the first half of 2005 primarily due to the reason provided above.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) increased $17.4 million during the second quarter of 2006 from $121.3 million at March 31, 2006 to $138.7 million at June 30, 2006. The increase was primarily related to additional case reserves for a healthcare transaction and an addition to loss adjustment expense reserves. Paid claims during the quarter amounting to $20.1 million included a payment on a CDO which had previously been classified within the active credit reserves, paid and terminated during the current quarter.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on adversely classified insured transactions. ***Ambac continuously monitors its insured portfolio actively seeking to mitigate claims.*** The ACR decreased by $24.7 million during the quarter, from $171.7 million at March 31, 2006 to $147.0 million at June 30, 2006. The decrease was primarily the result of net improvements in the classified portfolio and a transfer of ACR reserves to case reserves for the CDO transaction noted above. At June 30, 2006, the specific Hurricane Katrina-related provision amounts to $90.4 million, down slightly from $91.1 million at March 31, 2006. Approximately $1.1 billion of Katrina-impacted credits remain in Ambac's adversely classified credit portfolio. Ambac did not pay any Katrina-related claims during the quarter.

Other Items

Total net securities gains/(losses) for the second quarter of 2006 were $51.0 million, or $0.31 per diluted share; consisting of net realized gains on investment securities of $44.4 million, net mark-to-market gains on credit and total return derivatives of $7.2 million and net mark-to-market losses on non-trading derivative contracts of ($0.6) million. Approximately $3 8 million of the net realized gains on

investment securities relate to cash recoveries received during the quarter related to a security in the investment agreement portfolio that had been written down in 2002 and 2003. For the second quarter of 2005, net securities gains/(losses) were $29.6 million, or $0.14 per diluted share; consisting of net realized losses on investment securities of ($0.6) million, net mark-to-market losses on credit and total return derivatives of ($17.0) million and net mark-to-market gains on non-trading derivative contracts of $47.2 million. The mark-to-market gains on non-trading derivative contracts relate almost entirely to interest rate hedge contracts related to long-term fixed rate liabilities in Ambac's investment agreement business that were redesignated during that quarter. Those hedges were redesignated to meet the technical requirements of FAS 133 as of July 1, 2005.

Total net securities gains/(losses) for the first half of 2006 were $64.4 million, or $0.3 8 per diluted share; consisting of net realized gains on investment securities of $49.5 million, net mark-to-market gains on credit and total return derivatives of $14.4 million and net mark-to-market gains on non-trading derivative contracts of $0.5 million. For the first half of 2005 net securities gains were $38.8 million, or $0.19 per diluted share; consisting of net realized gains on investment securities of $1.3 million, mark-to-market losses on credit derivatives and total return swaps of ($10.9) million and net mark-to-market gains on non-trading derivative contracts of $48.4 million.

Balance Sheet

Highlights

Total assets as of June 30, 2006 were $20.27 billion, up 3% from total assets of $19.73 billion at December 31, 2005. The increase was driven by cash generated from operations during the period, partially offset by a decrease in unrealized gains in the investment portfolio driven by higher long-term interest rates.

As of June 30, 2006, stockholders' equity was $5.63 billion, a 5% increase from year-end 2005 stockholders' equity of $5.37 billion. The increase was primarily the result of net income during the period, offset by lower "Accumulated Other Comprehensive Income" driven by higher long-term interest rates.

(Emphasis added.)

32. On October 25, 2006, Ambac issued a press release entitled, "Ambac Financial Group, Inc. Announces Third Quarter Net Income of $213.5 Million, up 22%." The release further stated:

> Ambac Financial Group, Inc. (Ambac) today announced third quarter 2006 net income of $213.5 million, or $1.98 per diluted share. This represents a 22% increase from third quarter 2005 net income of $175.1 million, and a 23% increase in net income per diluted share from $1.61 in the third quarter of 2005.
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> Commenting on the overall results, Ambac Chairman and Chief Executive Officer, Robert J. Genader, noted, "I am pleased with the results given the challenging environment we have faced during much of the year. We are currently witnessing a solid level of deal inquiries and opportunities across most of our business segments. Domestic public finance, however, continues to pose a challenge given the decline in issuance and intensified pricing pressures. ***We remain steadfast in judiciously allocating our capital to transactions that enable us to continue to deliver superior returns.***"
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> Revenues
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> Highlights
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> Credit enhancement production in the third quarter of 2006 was $216.2 million, down 16% from the third quarter of 2005 which came in at $256.6 million. Growth in international was more than offset by declines in U.S. public finance and U.S. structured finance.
>
> Credit enhancement production for the nine months of 2006 of $980.7 million was 15% higher than credit enhancement production of $853.5 million in the same period of 2005, driven by growth in the international and U.S. structured finance markets during the nine-month period.
>
> Structured finance earned premiums and other credit enhancement fees grew 12%. The rate of growth in structured finance has improved as the recent level of writings in asset classes such as commercial asset-backed securities, auto securitizations and pooled debt obligations has increased. Narrow credit spreads and high prepayment speeds in the mortgage-backed and home equity book of business and early terminations of transactions in other structured finance sectors continue to partially offset the positive effects of new business writings.

International earned premiums and other credit enhancement fees decreased by 6%. The decline was driven primarily by significant paydowns and calls over the past several quarters and the recent business mix which has trended towards long dated infrastructure transactions that earn premiums over a longer period of time than typical structured finance exposures.

Net investment income (including net investment income from VIES) for the third quarter of 2006 was $120.2 million, representing an increase of 9% from $110.6 million in the comparable period of 2005. This increase was due primarily to growth in the investment portfolio driven by the ongoing collection of financial guarantee premiums and fees and a $200 million capital contribution from the parent company in the fourth quarter of 2005, partially offset by a $5.3 million net positive adjustment booked in the third quarter 2005 for municipal bonds within the portfolio that had been pre-refunded. Investment income from VIES is offset by interest expense on VIES, shown separately in the Consolidated Statements of Operations.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) decreased $12.0 million during the third quarter of 2006 from $13 8.7 million at June 30, 2006 to $126.7 million at September 30, 2006. The decrease was driven primarily by claim payments made during the quarter amounting to $8.9 million.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on adversely classified insured transactions. ***Ambac continuously monitors its insured portfolio actively seeking to mitigate claims.*** The ACR increased by $0.6 million during the quarter, from $147.0 million at June 30, 2006 to $147.6 million at September 30, 2006. The increase was driven by increased reserves on certain credits within the U.S. public finance and structured finance portfolios, offset by a $35.6 million reduction in the ACR for Hurricane Katrina impacted credits. At September 30, 2006, the specific Hurricane Katrina-related provision amounts to $50.5 million, down from $90.4 million at June 30, 2006. The decrease is primarily due to significant state and federal support recently provided to the region, particularly the greater New Orleans area. Ambac did not pay any Katrina-related claims during the quarter.

Provision for income taxes for the third quarter of 2006 amounted to $83.6 million, an effective tax rate of 28.1 %. This compares to the third quarter of 2005 tax provision of $51.9 million, an effective tax rate of 22.8%. The increased tax rate in 2006 was due to the net release of tax reserves in the third quarter 2005 and higher taxable income resulting

from improved financial guarantee underwriting results in the third quarter 2006 relative to the comparable prior period primarily as a result of Hurricane Katrina related loss activity.

Provision for income taxes for the nine months of 2006 amounted to $252.5 million, an effective tax rate of 27.3%. This compares to the nine months of 2005 tax provision of $193.1 million, an effective tax rate of 26.1 %. The increased tax rate in 2006 is explained above.

Other Items

Total net securities gains/(losses) for the third quarter of 2006 were $9.9 million, or $0.06 per diluted share; consisting of net realized gains on investment securities of $7.9 million, net mark-to-market gains on credit and total return derivatives of $2.1 million and net mark-to-market losses on non-trading derivative contracts of ($0.1) million. For the third quarter of 2005, net securities gains/(losses) were $14.5 million, or $0.08 per diluted share; consisting of net realized gains on investment securities of $9.5 million, net mark-to-market gains on credit and total return derivatives of $3.9 million and net mark-to-market gains on non-trading derivative contracts of $1.1 million.

Total net securities gains/(losses) for the nine months of 2006 were $74.4 million, or $0.44 per diluted share; consisting of net realized gains on investment securities of $57.5 million, net mark-to-market gains on credit and total return derivatives of $16.5 million and net mark-to-market gains on non-trading derivative contracts of $0.4 million. Approximately $51 million of the net realized gains on investment securities relate to cash recoveries received during the year related to a security in the investment agreement portfolio that had been written down in 2002 and 2003. For the nine months of 2005, net securities gains were $53.1 million, or $0.27 per diluted share; consisting of net realized gains on investment securities of $10.8 million, mark-to-market losses on credit derivatives and total return swaps of ($7.0) million and net mark-to-market gains on non-trading derivative contracts of $49.3 million. The mark-to-market gains on non-trading derivative contracts relate almost entirely to interest rate hedge contracts in Ambac's investment agreement business that were redesignated to meet the technical requirements of FAS 133 as of July 1, 2005.

Balance Sheet

Highlights

Total assets as of September 30, 2006 were $21.09 billion, up 7% from total assets of $19.73 billion at December 31, 2005. The increase was driven by cash generated from operations during the period.

As of September 30, 2006, stockholders' equity was $6.01 billion, a 12% increase from year-end 2005 stockholders' equity of $5.37 billion. The increase was primarily the result of net income during the period.

(Emphasis added.)

33. On January 31, 2007, the Company announced its fourth quarter 2006 results in a press release which stated, in relevant part:

Ambac Financial Group, Inc. (Ambac) today announced fourth quarter 2006 net income of $202.7 million, or $1.88 per diluted share. This represents a 1% decrease from fourth quarter 2005 net income of $204.3 million, or $1.90 per diluted share.

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Commenting on the overall results, Ambac Chairman and Chief Executive Officer, Robert J. Genader, noted, "I am satisfied with our overall business results for the quarter and for the full year. Despite one of the most difficult business environments the industry has faced in many years, Ambac's full-year top line production is very acceptable. Most gratifyingly, our record-level full-year international production demonstrates our success in expanding our global reach, as our triple-A financial strength and reputation for innovative and efficient execution is now firmly planted across a broad segment of the international markets."

Revenues

Highlights

Credit enhancement production in the fourth quarter of 2006 was $314.5 million, down 21% from the fourth quarter of 2005 which came in at $395.8 million. Growth in international was more than offset by declines in U.S. public finance and U.S. structured finance. Credit enhancement production for the full year of 2006 of $1,295.2 million was 4% higher than credit enhancement production of $1,249.4 million

in 2005, as significant growth in international business more than offset the decline in the U.S. public finance business.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) decreased $84.2 million during the fourth quarter of 2006 from $126.7 million at September 30, 2006 to $42.5 million at December 31, 2006. The decrease was driven by the settlement of several impaired transactions during the quarter including a health care transaction that had been fully-reserved. Total claim payments during the quarter amounted to $68.8 million.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on certain adversely classified insured transactions. Ambac continuously monitors its insured portfolio actively seeking to mitigate claims. The ACR increased by $25.0 million during the quarter, from $147.6 million at September 30, 2006 to $172.6 million at December 31, 2006. The increase was driven primarily by net increases in reserves on certain credits within the U.S. public finance portfolio, most notably within the transportation sector. At December 31, 2006, the specific Hurricane Katrina-related provision amounts to $50.1 million, down slightly from $50.5 million at September 30, 2006. Ambac did not pay any Katrina-related claims during the year.

Other Items

Total net securities gains/(losses) for the fourth quarter of 2006 were $5.8 million, or $0.04 per diluted share; consisting of net realized gains on investment securities of $9.6 million, net mark-to-market losses on credit and total return derivatives of ($4.8) million and net mark-to-market gains on non-trading derivative contracts of $1.0 million. For the fourth quarter of 2005, net securities gains/(losses) were $20.0 million, or $0.12 per diluted share; consisting of net realized losses on investment securities of ($2.2) million, net mark-to-market gains on credit and total return derivatives of $22.0 million and net mark-to-market gains on non-trading derivative contracts of $0.2 million.

Total net securities gains/(losses) for the full year of 2006 were $80.2 million, or $0.48 per diluted share; consisting of net realized gains on investment securities of $67.1 million, net mark-to-market gains on credit and total return derivatives of $11.6 million and net mark-to-market gains on non-trading derivative contracts of $1.5 million. Approximately $56 million of the net realized gains on investment securities in 2006 relate to cash recoveries received during

> the year related to a security in the investment agreement portfolio that had been written down in 2002 and 2003. For the full year of 2005, net securities gains were $73.1 million, or $0.40 per diluted share; consisting of net realized gains on investment securities of $8.6 million, mark-to-market gains on credit derivatives and total return swaps of $15.0 million and net mark-to-market gains on non-trading derivative contracts of $49.5 million. The mark-to-market gains on non-trading derivative contracts relate almost entirely to interest rate hedge contracts in Ambac's investment agreement business that were redesignated to meet the technical requirements of FAS 133 as of July 1, 2005.
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> Balance Sheet
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> Highlights
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> Total assets as of December 31, 2006 were $20.27 billion, up 9% from total assets of $18.55 billion at December 31, 2005. The increase was driven primarily by cash generated from operations during the period.
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> As of December 31, 2006, stockholders' equity was $6.18 billion, a 15% increase from year-end 2005 stockholders' equity of $5.38 billion. The increase was primarily the result of net income during the period.

(Emphasis added.)

34. On April 25, 2007, the Company announced its first quarter 2007 results in a press release which stated, in part:

> Ambac Financial Group, Inc. (Ambac) today announced first quarter 2007 net income of $213.3 million, or $2.02 per diluted share. This represents a 4% decrease from first quarter 2006 net income of $221.1 million, and a 2% decrease in net income per diluted share from $2.06 a year earlier.
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> Commenting on the overall results, Ambac Chairman and Chief Executive Officer, Robert J. Genader, noted, "The first quarter evidenced improved business production across all major business sectors relative to the 2006 comparable quarter. Debt issuance and capital markets activity continues to be strong. ***Importantly, recent evidence of credit spread widening in the mortgage related asset classes should lead to increased demand for our core financial guarantee product, provided of course, that wider spreads continue to prevail.***"

Revenues

Highlights

Credit enhancement production in the first quarter of 2007 was $310.1 million, up 33% from $233.5 million reported in the first quarter of 2006. Growth was achieved in all three sectors, led by the 49% increase in U.S. structured finance.

Reinsurance Cancellations

During the first quarter 2006, Ambac cancelled its remaining reinsurance contracts with two reinsurers and recaptured $3.9 billion ofpar outstanding. Included in ceded premiums in our Consolidated Statement of Operations is $37.0 million in returned premiums from the cancellations, of which approximately $29.3 million was deferred. The difference, $7.7 million, included in accelerated premiums, resulted from the difference between the contractual amount of returned premiums and the associated unearned premium remaining on the previously ceded portion of the underlying guarantees. The net income impact of the cancellations, presented in Table I, above, as part of accelerated premiums, amounted to approximately $2.0 million, or $0.02 per diluted share.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) decreased $4.8 million during the first quarter of 2007 from $42.5 million at December 31, 2006 to $37.7 million at March 31, 2007. The decrease was driven by improving conditions on certain credits for which we had previously paid claims. Total net claim payments during the quarter amounted to ($0.1) million.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on certain adversely classified insured transactions. The ACR increased by $16.2 million during the quarter, from $172.6 million at December 31, 2006 to $188.8 million at March 31, 2007. The increase was driven primarily by net increases in reserves on certain credits within the U.S. public finance portfolio.

Other Items

Total net securities gains/(losses) for the first quarter of 2007 were $3.7 million, consisting of net realized gains on investment securities of $6.6 million, net mark-to-market losses on credit and total return derivatives of ($1.9) million and net mark-to-market losses on non-trading derivative contracts of ($1.0) million. Approximately $6.2

million of the net realized gains on investment securities relate to cash recoveries received during the quarter related to a security in the investment agreement portfolio that had recognized impairment losses in prior years. For the first quarter of 2006, net securities gains/(losses) were $13.4 million, consisting of net realized gains on investment securities of $5.1 million, net mark-to-market gains on credit and total return derivatives of $7.2 million and net mark-to-market gains on non-trading derivative contracts of $1.1 million.

Balance Sheet

Highlights

Total assets as of March 31, 2007 were $20.11 billion, down 1% from total assets of $20.27 billion at December 31, 2006. The decrease was primarily driven by a net draw down from our investment agreement portfolio, partially offset by cash generated from operations during the period.

On February 12, 2007, Ambac issued $400 million of Directly-Issued Subordinated Capital Securities (DISCS(SM)). Ambac used the net proceeds from the offering and additional funds to purchase $400 million worth of shares of its common stock. The common stock was purchased through an accelerated share buyback agreement and resulted in 4.26 million shares acquired during the quarter. The total number of additional shares that will ultimately be repurchased under the program will be based on the volume-weighted average share price of the Company's common shares during the term of the accelerated buyback agreement.

As of March 31, 2007, stockholders' equity was $5.99 billion, a 3% decrease from year-end 2006 stockholders' equity of $6.18 billion. The decrease was primarily the result of the $400 million share buyback, partially offset by net income during the period.

(Emphasis added.)

35. Ambac's risk exposure related to CDOs first began to leak to the market with the announcement of the Company's second quarter 2007 results on July 25, 2007. Those results included losses of $56.9 million related to insured CDOs of asset-backed securities containing subprime mortgage-backed securities as collateral. However, Ambac downplayed its risk exposure to CDO risk, stating that "Ambac's exposure on those transactions all attach at

levels senior to the triple-A attachment points as established by the rating agencies." The release further stated:

> Ambac Financial Group, Inc. (Ambac) today announced second quarter 2007 net income of $173.0 million, or $1.67 per diluted share. This represents a 27% decrease from second quarter 2006 net income of $238.6 million, and a 25% decrease in net income per diluted share from $2.22. The decrease is primarily due to unrealized mark-to-market losses amounting to ($56.9) million, or ($0.36) per diluted share, related to credit derivative exposures in the second quarter 2007. The comparable quarter of 2006 included net realized gains on investment securities of $44.4 million, or $0.27 per diluted share, primarily resulting from cash recoveries received related to a security in the investment agreement portfolio that had been written down in prior years. ***The second quarter 2007 unrealized mark-to-market losses on credit derivative exposures is the result of unfavorable market pricing of collateralized debt obligations with significant amounts of sub-prime residential mortgage collateral.*** As further described below, net mark-to-market gains and losses on credit derivatives and net gains and losses from sales of investment securities are excluded from the earnings measures used by research analysts.
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> Commenting on the overall results, Ambac Chairman and Chief Executive Officer, Robert J. Genader, noted, "We are pleased with the breadth and quality of our business production in the quarter. ***Our rigorous and proven approach enabled us to deliver positive results despite the turmoil in the sub-prime mortgage market that resulted in a negative mark-to-market adjustment. Our triple-A business model offers us key advantages, including our ability to hold insured transactions to maturity; no collateral or margin requirements on transactions insured; and, in the unlikely event of default we pay scheduled principal and interest, thereby minimizing liquidity risk.***" Mr. Genader added, "Looking ahead, the disciplined execution of our strategy positions us well to benefit from the improving business conditions we see, with wider spreads, enhanced credit terms and increased demand for our valuable financial guarantee products."
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> Revenues
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> Highlights
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> Credit enhancement production in the second quarter of 2007 was $367.8 million, down 31% from Ambac's record quarterly production of $531.0 million reported in the second quarter of 2006.

Public finance earned premiums, before accelerations, grew 2% this quarter. Earned premium growth in this sector has been negatively impacted by the high level of refunding activity in Ambac's public finance book in recent years, competitive pricing and the mix of business underwritten in recent periods.

Structured finance earned premiums and other credit enhancement fees grew 10%. The rate of growth in structured finance has improved recently, driven by strong premium production in asset classes such as pooled debt obligations and commercial asset-backed securities over the past several quarters.

International earned premiums and other credit enhancement fees decreased 2%. The decrease has resulted from deal terminations and a slow down in deal closings in 2007 relative to the prior year.

Net investment income for the second quarter of 2007 was $113.2 million, representing an increase of 8% from $104.5 million in the comparable period of 2006. This increase was due primarily to growth in the investment portfolio driven by the ongoing collection of financial guarantee premiums and fees.

Net investment income for the six months of 2007 was $225.3 million, representing an increase of 9% from $206.2 million in the comparable period of 2006, primarily as a result of the reasons provided above.

Financial services revenues. The financial services segment is comprised of the investment agreement business and the derivative products business. Gross interest income less gross interest expense from investment and payment agreements plus results from the derivative products business, excluding net realized investment gains and losses and unrealized gains and losses on total return swaps and nontrading derivative contracts, was $9.2 million in the second quarter of 2007, down 15% from $10.8 million in the second quarter of 2006. The decrease was primarily due to lower revenue from the interest rate swap, total return swap and investment agreement businesses in the second quarter 2007.

Financial services revenues were $19.9 million in the first half of 2007, down 12% from the $22.5 million of revenues in the first half of 2006 primarily due to the reason provided above.

Expenses

Highlights

Financial guarantee expenses of $50.5 million for the second quarter of 2007 increased 13% from $44.7 million of expenses for the second quarter of 2006. Financial guarantee loss and loss expenses were $17.1 million in the second quarter of 2007, up from $12.8 million in the second quarter of 2006. See "Loss Reserve Activity," below, for additional information on losses. Net underwriting and operating expenses of the financial guarantee sector totaled $33.4 million in the second quarter of 2007, up 5% from $31.9 million in the second quarter of 2006 primarily due to increased compensation expense.

Financial guarantee expenses of $98.3 million for the first six months of 2007 increased 19% from $82.7 million of expenses for the same period of 2006. The increase results primarily from higher loss expenses during the period.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) increased $9.6 million during the second quarter of 2007 from $37.7 million at March 31, 2007 to $47.3 million at June 30, 2007. Included in the March 31, 2007 case reserves balance were offsetting receivables for claims previously paid on a European transportation transaction that were deemed by management to be recoverable upon the anticipated successful restructuring of that transaction. The restructuring was finalized during the quarter and the payments due to Ambac were received. Total net claim payments/(receipts) during the quarter amounted to ($7.5) million.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on certain adversely classified insured transactions. The ACR increased by $14.9 million during the quarter, from $188.8 million at March 31, 2007 to $203.7 million at June 30, 2007. ***The increase was driven primarily by increases in reserves on certain credits primarily within the transportation sector of the U.S. public finance portfolio and to a lesser extent within the non-subprime RMBS sector of the structured finance portfolio, partially offset by favorable credit activity throughout both portfolios.***

Other Items

Total net securities gains/(losses) for the second quarter of 2007 were ($52.7) million, consisting of net realized gains on investment

securities of $1.2 million, net mark-to-market losses on credit and total return derivatives of ($57.9) million and net mark-to-market gains on non-trading derivative contracts of $4.0 million. ***During the quarter a net mark-to-market loss amounting to ($56.9) million was recorded related to insured collateralized debt obligations of asset-backed securitizations containing sub-prime mortgage-backed securities as collateral. The negative mark-to-market is driven by current market concerns over the most recent vintages of subprime RMBS and the recent lack of liquidity in the CDO of ABS market resulting in a reduction in market-quoted prices. Ambac's exposure on those transactions all attach at levels senior to the triple-A attachment points as established by the rating agencies.***

For the second quarter of 2006, net securities gains/(losses) were $51.0 million, consisting of net realized gains on investment securities of $44.4 million, net mark-to-market gains on credit and total return derivatives of $7.2 million and net mark-to-market losses on non-trading derivative contracts of ($0.6) million. Approximately $38 million of the second quarter 2006 net realized gains on investment securities related to cash recoveries received from a security in the investment agreement portfolio that had been written down in previous years.

Total net securities gains/(losses) for the first half of 2007 were ($49.0) million, consisting of net realized gains on investment securities of $7.8 million, net mark-to-market losses on credit and total return derivatives of ($59.8) million and net mark-to-market gains on non-trading derivative contracts of $3.0 million. For the first half of 2006 net securities gains were $64.4 million, consisting of net realized gains on investment securities of $49.5 million, net mark-to-market gains on credit and total return derivatives of $14.4 million and net mark-to-market gains on nontrading derivative contracts of $0.5 million.

Balance Sheet

Highlights

Total assets as of June 30, 2007 were $21.06 billion, up 4% from total assets of $20.27 billion at December 31, 2006. The increase was primarily driven by cash generated from operations during the period, partially offset by a decrease in unrealized gains in the investment portfolio due to a rise in long-term interest rates.

As of June 30, 2007, stockholders' equity was $6.04 billion, a 2% decrease from year-end 2006 stockholders' equity of $6.18 billion. The decrease was primarily the result of the $400 million share buyback and lower Accumulated Other Comprehensive Income driven by higher long-term interest rates, partially offset by net income during the period.

> During the second quarter 2007, Ambac completed the buyback of $400 million of its common stock under its accelerated share buyback program (originally announced on February 12, 2007). The total number of shares purchased under the agreement amounted to 4.46 million shares. Ambac also bought back 194 thousand shares of its common stock at a total cost of $16.9 million during the second quarter that was unrelated to the accelerated share buyback program.

(Emphasis added.)

36. Following this revelation, on July 26, 2007, Ambac's stock dropped by $3.85 per share to close at $75.56 per share, a one-day decline of 5% on volume of more than 4 million shares.

37. To reassure investors with the false appearance of transparency concerning its CDO exposure, Ambac issued a press release on August 10, 2007 stating that it would provide detailed information on its website "regarding its exposure to Collateralized Debt Obligations of Asset-backed Securities ("CDOs of ABS"), including additional details of each transaction's underlying collateral composition, underlying collateral ratings, and overall transaction ratings." However, the information Ambac provided was incomplete and misleading as to the true extent of Ambac's CDO exposure.

38. Nonetheless, on this partial disclosure Ambac's stock declined by an additional $3.15 per share to close at $62.99 per share, a one-day drop of 5% on volume of 4.7 million shares.

39. On September 10, 2007, Ambac announced that it had updated its website's information concerning Ambac's CDO exposure, including "refreshed Ambac ratings and a summary of the results of a detailed analysis of the underlying collateral related to three CDO transactions executed in 2007." However, the information Ambac provided continued to misrepresent Ambac's exposure.

40. On October 10, 2007, Ambac announced that it would be realizing a loss in the third quarter 2007 in the amount of $743 million related to its credit derivative contracts. The release stated, in relevant part:

> Ambac Financial Group, Inc. (Ambac) today announced the results of its third quarter fair value review of its outstanding credit derivative contracts. Ambac's estimate of the fair value or "mark-to-market" adjustment for its credit derivative portfolio at September 30, 2007 amounted to an ***unrealized loss of $743 million***, pre-tax. The company expects to report a net loss per diluted share up to $3.50 in the third quarter. Earnings measures reported by research analysts are on an operating basis and exclude the net income impact of mark-to-market gains and losses on credit derivative contracts, as well as certain other items. The company expects to report positive operating earnings per diluted share between $1.85 and $1.90 in the third quarter.
>
> Commenting on the estimated result, Ambac Chairman and Chief Executive Officer, Robert J. Genader, stated, "While this unrealized loss is disappointing, it is important to note that Ambac's credit derivative contracts are similar to our insurance policies in that neither is exposed to the liquidity risks that are typically embedded in standard derivative contracts." Mr. Genader added, ***"While the turmoil in the structured finance markets has resulted in this unfavorable unrealized mark-to-market for the quarter, we have observed significantly improved market conditions for the industry and I am encouraged by the recent increased interest in our core financial guaranty product. Moreover, I remain confident in our underwriting abilities, credit standards and the transactions we have insured."***
>
> Ambac Senior Vice President and Chief Financial Officer, Sean Leonard, noted, "***Ambac does not view the current adjustments as predictive of future claims. Indeed, the average internal credit rating of our derivative portfolio is AA+ at September 30, 2007 and based on our recent analysis of the portfolio, management believes that the potential for material paid claims is very low. Importantly, the company's claims paying resources, as prescribed by the rating agencies, are not impacted by mark-to-market adjustments***."
>
> The company also expects to report the following for the third quarter of 2007: (i) loss provision of approximately $20 million; (ii) estimated accelerated premiums from refundings, calls and other accelerations of approximately $16 million; (iii) credit enhancement production of approximately $430 million; and (iv) Ambac's highly rated investment portfolios, which total to approximately $19 billion, are

> expected to have net embedded unrealized gains of approximately $100 million as of September 30, 2007.

(Emphasis added.)

41. On October 24, 2007, Ambac released its third quarter 2007 results which stated, in relevant part:

> Ambac Financial Group, Inc. (Ambac) today announced a third quarter 2007 net loss of ($360.6) million, or ($3.51) per diluted share. This compares to third quarter 2006 net income of $213.5 million, or net income per diluted share of $1.98. ***The decrease is due to the previously announced unrealized loss on credit derivative exposures amounting to ($743.4) million, or ($5.29) per diluted share in the third quarter 2007. The third quarter 2007 unrealized mark-to-market loss on credit derivative exposures was discussed in a press release dated October 10, 2007, and is primarily the result of unfavorable market pricing of collateralized debt obligations.*** As further described below, net mark-to-market losses on credit derivatives are excluded from the earnings measures used by research analysts.
>
> ***
>
> Commenting on the overall results, Ambac Chairman and Chief Executive Officer, Robert J. Genader, noted, "***We have observed improved overall market conditions in most asset classes of our core financial guaranty product, despite the recent turmoil in the structured finance markets.*** Business production during the quarter was quite robust, reflective of both a strong pipeline and better overall pricing in the current market." Mr. Genader added, ***"With regard to the sizable mark-to-market adjustment recorded in the quarter, it is important to note that Ambac's credit derivative contracts, like our insurance policies, are not exposed to the type of liquidity risk that is typically embedded in standard derivative contracts."***
>
> Revenues
>
> Highlights
>
> Credit enhancement production in the third quarter of 2007 was $431.1 million, up 99% from Ambac's production of $216.2 million reported in the third quarter of 2006.
>
> Credit enhancement production for the nine months of 2007 of $1,109.1 million was 13% higher than credit enhancement production of $980.7 million in the same period of 2006.

Loss Reserve Activity

Case basis loss reserves (loss reserves for exposures that have defaulted) increased $59.8 million during the third quarter of 2007 from $47.3 million at June 30, 2007 to $107.1 million at September 30, 2007. The increased case reserves relate primarily to two RMBS transactions that are underperforming original expectations. Total net claim receipts during the quarter amounted to $3.7 million.

Active credit reserves ("ACR") are established for probable and estimable losses due to credit deterioration on certain adversely classified insured transactions. The ACR decreased by $37.0 million during the quarter, from $203.7 million at June 30, 2007 to $166.7 million at September 30, 2007. The reserve decline was driven by net favorable credit activity, primarily within the public finance portfolio, partially offset by increased reserves within the RMBS sector of the structured finance portfolio.

Other Items

Total net securities gains/(losses) for the third quarter of 2007 were ($757.2) million, consisting of net realized gains on investment securities of $4.2 million, net mark-to-market losses on credit and total return derivatives of ($756.3) million and net mark-to-market losses on non-trading derivative contracts of ($5.1) million. ***During the quarter a net mark-to-market loss amounting to ($743.4) million was recorded related to contracts executed in credit default format, primarily in our collateralized debt obligation exposures. The negative mark-to-market is driven by dramatically lower prices in certain structured finance asset classes. The lower prices were driven by uncertainty regarding the ultimate outcome of subprime losses.*** Reduced demand for certain structured asset classes, a lack of liquidity in the markets, forced selling by structured and/or leveraged investment vehicles, all combined to exacerbate pricing declines across the structured debt capital markets.

For the third quarter of 2006, net securities gains/(losses) were $9.9 million, consisting of net realized gains on investment securities of $7.9 million, net mark-to-market gains on credit and total return derivatives of $2.1 million and net mark-tomarket losses on non-trading derivative contracts of ($0.1) million.

Total net securities gains/(losses) for the first nine months of 2007 were ($806.0) million, consisting of net realized gains on investment securities of $12.0 million, net mark-to-market losses on credit and total return derivatives of ($816.0) million and net mark-to-market losses on non-trading derivative contracts of ($2.0) million. For the first nine months of 2006 net securities gains were $74.4 million, consisting of net

> realized gains on investment securities of $57.5 million, net markto-market gains on credit and total return derivatives of $16.5 million and net markto-market gains on non-trading derivative contracts of $0.4 million. Approximately $51 million of the 2006 net realized gains on investment securities related to cash recoveries received during the year related to a security in the investment agreement portfolio that had been written down in previous years.
>
> Balance Sheet
>
> Highlights
>
> Total assets as of September 30, 2007 were $21.97 billion, up 8% from total assets of $20.27 billion at December 31, 2006. The increase was primarily driven by cash generated from operations during the period, partially offset by a decrease in unrealized gains in the investment portfolio due to a rise in long-term interest rates.
>
> As of September 30, 2007, stockholders' equity was $5.65 billion, a 9% decrease from year-end 2006 stockholders' equity of $6.18 billion. The decrease was primarily the result of the $400 million share buyback earlier in the year and lower Accumulated Other Comprehensive Income driven by higher long-term interest rates.

(Emphasis added.)

42. Following this partial disclosure, Ambac's stock dropped by 9% to close that day at $51.00 per share on volume of 10.8 million shares. Ambac's stock continued its free-fall the next day, closing down another $7.05 per share at $43.95, a one-day decline of 14% on volume of 16.4 million shares.

43. On November 2, 2007, Morgan Stanley issued a report on the financial guaranty industry which lowered the financial guarantee industry to "in-line" from "attractive" and raised concerns that additional losses at Ambac could force the Company to raise capital to protect its triple-A rating.

44. Upon this news, Ambac's share price fell $6.06 per share to close at $23.51, a one-day decline of 20.5% on volume of 29.9 million shares.

45. Ambac attempted to refute the Morgan Stanley report in a press release on November 6, 2007, in which the Company stated:

> "Questions Arise on Mark to Market Losses"
>
> On page 6 the analyst states, "One of the first negative surprises we saw last week stemmed from the large discrepancy between the mark-to-market losses reported by the financial guarantors and Merrill Lynch."
>
> Management Comment:
>
> It is difficult for us to comment on the Merrill Lynch mark-to-market loss as we do not have any visibility into their transactions. Without such details on Merrill's book, one can only speculate as to the differences in the portfolios.
>
> Several differences may exist between exposures contained in Ambac's portfolio and an investment bank's portfolio and therefore may influence the estimated mark of the different portfolios. For example, we have noted that later vintage high-grade ABS CDOs (particularly those with 2007 and late 2006 vintage underlying collateral) and high-grade ABS CDOs that have large inner CDO components, have suffered more severe mark-to-market losses. Additionally, as one might expect, the amount of first loss subordination and credit migration triggers present in a structure also can impact the market value of the senior tranche. Finally, the terms of the contract may also impact the estimate of fair value. Ambac's Credit Default Swap ("CDS") contracts are highly modified from a standard CDS used by investment banks. Ambac CDS contracts do not include collateral posting provisions, and are generally limited to payment shortfalls of interest and principal. Ambac's contract terms are significant variations from standard CDS contracts and have significant value, particularly in difficult markets. In fact, certain investment banks will not enter into an Ambac CDS due to the favorable nature (towards Ambac) of its terms.
>
> Some background on Ambac's mark-to-market follows. The mark-to-market unrealized loss is an estimate of our CDS contracts' "fair value". It is an estimate because our CDS contract does not trade in any market. Under U.S. generally accepted accounting principles, CDS contracts must be recorded at fair value. Fair value is defined broadly as the price that a contract could be settled in a current transaction between willing parties, other than in a forced or liquidation sale.
>
> Because an estimate of fair value of a CDS contract includes many market factors, an unrealized loss may not result in an increased

expectation of loss. A good example of this dynamic is a general decline in the level of liquidity (witnessed by fewer buyers in the market) for a particular asset or asset class. Ambac believes that only through rigorous analytics of the actual transaction and its attributes and protections, as well as performance to date and expected future performance of underlying collateral, will one obtain meaningful information on the potential for actual losses.

Most all-major financial institutions are struggling with this issue. Particularly institutions where the process of marking-to-market is a critical part of operations, such as those that need to calculate required collateral postings. We are subject to information that we receive from market participants, which are primarily comprised of major investment banking institutions. Given the lack of liquidity in the market, the potential for CDO downgrading activity by the rating agencies, the potential for forced selling by other investors (due to downgrades), and the overall uncertainty surrounding the ultimate outcome of the subprime mortgage market, Ambac does expect significant volatility in the mark-to-market of its CDO portfolio for the foreseeable future.

"CDO Downgrades Have Started"

On pages 6 and 7, the analyst discusses the recent internal rating downgrades of certain AB S CDOs. He states "If they were to downgrade the securities further, we would be highly disappointed and expect investor confidence in management to be strained."

Management Comment:

Ambac has a rigorous surveillance process surrounding its entire book of business. Management has subjected the mortgage and ABS CDO books to more frequent and more detailed reviews in the current environment. We believe this is prudent and responsible given the current stressed credit environment surrounding the mortgage market. While Ambac underwrites its transactions to withstand significant stress, the underlying credit rating is impacted by expected unfavorable collateral performance. To date, the downgrades noted in the subject transactions are within the parameters of Ambac's original stress tests. Ambac's independent Surveillance and Risk Management group determine the deal ratings. The ratings are based on the performance observed to date and a projection of future performance of the underlying collateral. Given the significant stress in the mortgage market, it should not be surprising that there have been downgrades. We are highly confident in our ratings process. Over time, as new information becomes available and as performance data is analyzed, we will adjust ratings up or down accordingly.

"Increasing Our Expectation of CDO Losses"

The analyst states, "We are increasing our CDO loss expectations for both Ambac and MBIA to reflect an updated tally of various market opinions about cumulative sub prime losses."

Management Comment:

It appears that the "various market opinions" referred to in the analyst's report relate to the 2006 and early 2007 vintage sub prime. It also appears that he is assuming that the Ambac ABS CDO book will reflect the performance of the ABX index of 2006 and 2007 vintage sub prime collateral and ignores the actual vintage diversification and asset quality triggers inherent in Ambac's book. We see wide differences in the market regarding the estimate of ultimate cumulative loss for the 2006 and early 2007 vintage. We typically hear a range from 8% to 17% with a wide dispersion around the mean. We understand the three major rating agencies are projecting a range of 10% to 14%. One of the rating agencies recently reported estimates with significant differences dependent upon vintage. There were notable differences between the first half of 2006 and more recent vintages. We believe this is a critical point that is missed by simply applying a broad 15% estimated cumulative loss across the book of business. It does not compensate for vintage dispersion inherent in our transactions, nor does it factor in different rating and FICO segmentation. Additionally, many of the ABS CDOs contain 2005 vintage mortgages, including Ambac transactions that were underwritten in 2007. That vintage is performing significantly better than 2006 and 2007. This illustrates the over simplification of applying a single cumulative loss across the board.

"Becoming More Conservative with Capital"

The analyst states, "We can not help but think that if management truly believed losses are unlikely, they would be willing to make a stronger statement with how they manage their capital (i.e. increased share buybacks)."

Management Comment:

As management has stated many times in the past, Ambac manages its capital levels to a triple-A standard. That requires us to be very cautious with capital levels, particularly in times of credit stress. For instance, a transaction rated AA will attract more capital than a similar transaction rated AAA. It is unlikely claims will be paid under either transaction. The global capital markets and virtually all major financial institutions are in the midst of a major credit and liquidity crunch. There is uncertainty regarding the ultimate outcome of losses in

> the U.S. mortgage market, concerns over leveraged investment vehicles and overall concern that the problems surrounding the mortgage market will adversely impact other sectors of the economy. Such an environment has caused credit spreads in many sectors to widen significantly. This environment provides both opportunities and limitations for Ambac. With regard to opportunities, returns on business written are up sharply in many sectors and we have seen a notable increase in attractive opportunities to put our capital to work for our shareholders. With regard to limitations, the market environment has caused some fixed income investors to have increased concern about the financial guaranty industry. As a result, all of the major participants in the industry have seen their credit spreads widen significantly. We believe applying capital to high return business and at the same time maintaining a stronger balance sheet by holding off on share repurchases is a responsible course in the current environment and one that meets our objective of managing our capital consistent with a triple-A standard. We believe this prudent strategy is good for both our equity and fixed income investors and will help restore confidence in our industry.
>
> Summary comments:
>
> We certainly understand the heightened concerns summarized in the analyst's report. Most all participants in the financial markets, including Ambac have a heightened concern over the ultimate outcome of the U. S. mortgage market. However, ***we are confident in the quality of our internal credit ratings process. We have been very transparent to the market and our investors by disclosing significant detail on our direct mortgage and CDO exposure in our various public disclosures. We have a rigorous and current review and rating process in place and we will react quickly as projected collateral performance changes.***

(Emphasis added.)

46. Following this release, Ambac's share price partially rebounded to close at $27.99 on November 6, 2007.

47. However, on November 27, 2007, Ambac executives announced at a Banc of America securities bond insurer conference that the Company was considering raising capital through reinsurance or sales of debt or stock in order to maintain the Company's triple-A rating. Upon this news, Ambac's shares fell by approximately 9% from the prior day to close at $21.79 on volume of over 12 million shares.

48. On December 17, 2007, Moody's Investors Service ("Moody's") announced that, following its review of Ambac's capital position, it was affirming Ambac's triple-A rating and maintaining a "stable" outlook for the Company.

49. Following Moody's announcement, Ambac issued a press release entitled, "Ambac's Aaa Rating is Affirmed, Outlook Stable," stating that "Ambac is pleased by this result which underscores the strength of our portfolio. We are optimistic about the business opportunities ahead and we will strategically explore these opportunities while remaining absolutely committed to preserving our triple-A rating." Ambac's shares closed at $26.66 on volume of almost 18 million shares that day, up $3.85 from the closing price on the prior trading day.

50. On December 19, 2007, S&P announced that it was affirming Ambac's triple-A rating but changing its outlook for the Company from "stable" to "negative," indicating that Ambac's triple-A credit rating would be at a heightened risk of being cut in the next two years due to deteriorating mortgage debt.

51. Following this announcement, Ambac commented, "We are confident the performance of our insured portfolio and the measures being taken to expand Ambac's capital position will be sufficient to return our outlook to stable."

52. On December 21, 2007, Fitch announced its completion of a review of Ambac's CDO and residential mortgage-backed securities portfolio, stating that the Company would be required to increase its capital reserves by $1 billion in order to maintain its triple-A credit rating with the agency. Specifically, the triple-A rating of Ambac's bond insurance unit was placed on "Rating Watch Negative, which means the agency will downgrade to AA+ in four to six weeks unless the company can boost [its] excess capital levels before then."

53. Later that day, Ambac commented on Fitch's action, stating that "The Fitch announcement concludes this phase of the rating agencies' reviews. As previously stated, Ambac has been investigating solutions to expand its capital position. Between our own analysis and that of the rating agencies, we are now in a better position to make informed, disciplined decisions regarding the form and timing of capital expansion."

54. On January 16, 2008, Ambac issued a press release announcing, *inter alia*, its preliminary fourth quarter 2007 results.[1] Ambac estimated a net loss of $3.4 billion for the fourth quarter, including a mark-to-market loss of $5.4 billion related to the Company's credit derivatives portfolio. Approximately $1.1 billion of that loss was attributed to CDO backed by subprime residential mortgage-backed securities. The release stated:

> (Ambac) today announced that its Board of Directors has approved a plan to strengthen its capital base through the issuance of at least $1 billion of equity and equity-linked securities. This plan may also include additional capital from reinsurance or issuance of debt securities. Ambac said that it is committed to maintaining its triple-A financial strength. By raising at least $1 billion in capital, Ambac is expected to meet or exceed Fitch Ratings' current triple-A capital requirements for the Company. The Company noted that its existing capital position currently meets or exceeds the triple-A capital requirements of both S&P and Moody's. As part of its capital initiative, Ambac also said that it will reduce the quarterly dividend on its common stock from $0.21 per share to $0.07 per share.
>
> Management Change
>
> Ambac's Board of Directors announced today that it has named Michael A. Callen as Chairman and Interim Chief Executive Officer. Mr. Callen has been Presiding Director and a member of the Audit; Compensation; and Governance committees of Ambac's Board of Directors. He succeeds Robert J. Genader, who will retire from the

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[1] On January 22, 2008, the Company released its final fourth quarter 2007 results, which came in slightly higher than the preliminary numbers announced on January 16th. The net loss reported was $3.3 billion, $31.85 per share, including $5.2 billion in mark-to-market losses related to Ambac's credit derivatives portfolio. The amount attributed to CDOs backed by subprime residential mortgage-backed securities remained the same, at approximately $1.1 billion.

Company effective today. "Mike has extensive experience in advising and leading companies engaged in sophisticated capital markets transactions, and he will provide valuable leadership to the excellent management team at Ambac," said Jill Considine, Chairman of the Board's Governance Committee. Ms. Considine commented further, "On behalf of the Board and everyone at Ambac, I would like to thank Bob Genader for his more than 20 years of dedication to Ambac. He has served the Company in almost every capacity throughout his long career, and has been a true asset. Indeed, one of the most important testaments to his leadership is the highly-qualified management team currently at Ambac. We wish him well in his retirement."

Mr. Callen said, "We have great confidence in our plan to enhance Ambac's capital position by over $1 billion within an accelerated time frame. We are optimistic about the long-term business opportunities ahead for Ambac, even as we respond to the volatility in the present credit market. We expect that our experienced management team, significant size and scale, and expertise in growing market sectors such as global infrastructure finance will help us tap the potential of the market today and into the future." Mr. Callen also stated that the Company has been working with Credit Suisse as its financial adviser.

Mark-to-market and Losses

The Company also announced the results of its fourth quarter fair value review of its outstanding credit derivative contracts. Ambac's estimate of the fair value or "mark-to-market" adjustment for its credit derivative portfolio for the quarter ended December 31, 2007 amounted to an estimated loss of $5.4 billion, pre-tax, $3.5 billion, after tax. ***Of the estimated $5.4 billion pre-tax mark-to-market loss, approximately $1.1 billion represents estimated credit impairment related to certain collateralized debt obligations of asset-backed securities transactions. These transactions are backed primarily by mezzanine level subprime residential mortgage-backed securities that have been internally downgraded to below investment grade. Ambac continues to believe that the balance of the mark-to-market losses taken to date are not predictive of future claims and that, in the absence of further credit impairment, the cumulative marks would be expected to reverse over the remaining life of the insured transactions.***

Ambac also expects to report a loss provision amounting to approximately $143 million, pre-tax. The loss provision relates primarily to underperforming home equity line of credit and closed-end second lien RMBS securitizations.

As a result of the aforementioned losses, Ambac expects to report a net loss per share of up to $32.83 for the fourth quarter ended December

> 31, 2007. Earnings measures reported by research analysts are on an operating basis and exclude the net income impact of mark-to-market gains and losses on credit derivative contracts internally rated investment grade, as well as certain other items. Ambac expects to report operating losses (1) per share of up to $5.80 for the fourth quarter primarily as a result of the aforementioned losses on CDOs and home equity line of credit transactions. In addition, book value per share is expected to be approximately $21.00 per share at December 31, 2007.

55. Later that same day, Moody's announced it was putting Ambac's AAA rating on review for possible downgrade.

56. In response to the news from Ambac and Moody's, Ambac's share price plummeted on January 16, 2008, to close at $12.97, a 38% decline from the prior day's closing price of $21.14.

57. On January 17, 2008, Ambac commented on Moody's announcement, stating, "In view of the uncertainty generated by Moody's surprising announcement, Ambac is assessing the impact of this action on the Company's previously announced capital plan."

58. Following this announcement, Ambac's share price fell to a new 52-week low of $4.50, rebounding only slightly to close at $6.24 per share on unprecedented volume of almost 62.8 million shares.

59. On January 18, 2008, Ambac announced that it would not be raising $1 billion in equity to shore up its capital position, as previously announced. As a result, later that same day Fitch downgraded Ambac from AAA to AA. Additionally, S&P put Ambac's rating on review for possible downgrade.

60. Following these announcements, Ambac's share price dropped further, to close at $6.20 on January 18, 2008.

61. The above statements issued by Defendants during the Class Period were materially false and misleading when made for the following reasons:

a. Ambac's internal controls and risk management practices were inadequate, causing the Company's loss projections and financial results reported during the Class Period to be misstated;

b. Ambac's financial statements were materially misstated due to its failure to properly account for the mark-to-market losses relating to its CDOs, MBSs and credit default swaps;

c. Given the deterioration and increased volatility of the mortgage market, Ambac would be forced to tighten its underwriting practices for structured finance products, including CDOs and MBSs, which would have a material, negative impact on its revenues from premiums going forward;

d. Ambac had far greater exposure to anticipated losses and defaults related to its CDOs, including its highly rated CDOs, than it had previously disclosed, and;

e. Defendants' statements about the Company's selective underwriting practices concerning CDOs and other structured finance products belied the true, aggressive and inadequate underwriting practices employed by the Company during the Class Period.

62. These misrepresentations caused Ambac's stock to trade at inflated prices – as high as $96.08 as of May 2007 – and allowed certain Individual Defendants to reap approximately $68 million in proceeds on the sale of their shares. However, when the truth ultimately was revealed, Ambac's share price plummeted to $6.20 per share, a 93% drop from the high price of $96.08.

63. As a result of their purchases of Ambac's securities during the Class Period, plaintiff and other members of the Class suffered economic loss, *i.e.*, damages under the federal securities laws.

FRAUD-ON-THE-MARKET DOCTRINE

64. At all relevant times, the market for Ambac common stock was an efficient market for the following reasons, among others:

a. the Company's common stock met the requirements for public listing and was listed and actively traded on the NASDAQ National Exchange, a highly efficient market;

b. as a regulated issuer, the Company filed periodic public reports with the SEC, and;

c. the Company regularly issued press releases which were carried by national news wires. Each of these releases was publicly available and entered the public marketplace.

65. As a result, the market for the Company's common stock promptly digested current information with respect to Ambac from all publicly available sources and reflected such information in the price of the Company's common stock. Under these circumstances, all purchasers of the Company's publicly traded common stock during the Class Period suffered similar injury through their purchase of the publicly traded common stock of Ambac at artificially inflated prices and a presumption of reliance applies.

ADDITIONAL SCIENTER ALLEGATIONS

66. As alleged herein, Defendants acted with scienter in that Defendants knew that the public documents and statements issued or disseminated in the name of the Company were materially false and misleading; knew that such statements or documents would be issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements or documents as primary violations of the federal securities laws. As set forth elsewhere herein in detail, Defendants, by virtue of their

receipt of information reflecting the true facts regarding Ambac, their control over, and/or receipt and/or modification of Ambac's allegedly materially misleading misstatements and/or their associations with the Company which made them privy to confidential proprietary information concerning Ambac, participated in the fraudulent scheme alleged herein.

67. Defendants knew or recklessly disregarded the falsity and misleading nature of the information which they caused to be disseminated to the investing public. The ongoing fraudulent scheme described in this complaint could not have been perpetrated over a substantial period of time, as has occurred, without the knowledge and complicity of the personnel at the highest level of the Company, including the Individual Defendants.

68. Defendants had the motive and opportunity to perpetrate the fraudulent scheme and course of business described herein because during the Class Period and with Ambac's stock trading at an inflated price, company insiders sold over $68.8 million dollars' worth of Ambac stock, as described more particularly below:

NAME	TIME PERIOD	SHARES SOLD	PROCEEDS
Robert J. Genader	11/02/2005-04/27/2007	314,932	$26,432,261.57
Phillip B. Lassiter	11/07/2005-02/22/2007	486,459	40,507,318.96
Thomas J. Gandolfo	05/03/2006-02/09/2007	21,625	1,891,577.47
	TOTALS:	**823,016**	**$68,831,158.00**

NO SAFE HARBOR

69. The statutory safe harbor provided for forward-looking statements under certain circumstances does not apply to any of the allegedly false statements pleaded in this complaint. To the extent there were any forward-looking statements, there were no meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the purportedly forward-looking statements. Alternatively, to the extent that the statutory

safe harbor does apply to any forward-looking statements pleaded herein, Defendants are liable for those false forward-looking statements because at the time each of those forward-looking statements was made, the particular speaker knew that the particular forward looking statement was false, and/or the forward-looking statement was authorized or approved by an executive officer of Ambac, who knew that those statements were false when made.

CLAIMS FOR RELIEF

COUNT I

(Violation of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder, Against All Defendants)

70. Plaintiff incorporates ¶¶1-69 by reference.

71. During the Class Period, Defendants disseminated or approved the false statements specified above, which they knew or recklessly disregarded were materially false and misleading in that they contained material misrepresentations and failed to disclose material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

72. Defendants violated Section 10(b) of the 1934 Act and Rule 10b-5 in that they:

a. Employed devices, schemes and artifices to defraud;

b. Made untrue statements of material facts or omitted to state material facts necessary in order to make statements made, in light of the circumstances under which they were made not misleading; or

c. Engaged in acts, practices, and a course of business that operated as a fraud or deceit upon Plaintiff and others similarly situated in connection with their purchases of Ambac securities during the Class Period.

73. Plaintiff and the Class have suffered damages in that, in reliance on the integrity of the market, they paid artificially inflated prices for Ambac securities. Plaintiff and the Class would not have purchased Ambac securities at the prices they paid, or at all, if they had been aware that the market prices had been artificially and falsely inflated by Defendants' misleading statements.

74. As a direct and proximate result of these Defendants' wrongful conduct, Plaintiff and the other members of the Class suffered damages in connection with their purchases of Ambac securities during the Class Period.

COUNT II

(Violation of Section 20(a) of the 1934 Act, Against Individual Defendants)

75. Plaintiff incorporates ¶¶1-69 by reference.

76. The Individual Defendants, by virtue of their offices, directorship, and specific acts were, at the time of the wrongs alleged herein, controlling persons of the Company within the meaning of Section 20(a) of the Exchange Act. The Individual Defendants had the power and influence and exercised the same to cause the Company to engage in the illegal conduct and practices complained of herein by causing the Company to disseminate to the public, or through analysts, the materially false and misleading information referred to above.

77. The Individual Defendants' positions made them privy to, and provided them with, actual knowledge of the material facts concealed from plaintiff and the Class by the Company during the Class Period.

78. By reason of the conduct alleged in the Count I, the Individual Defendants are liable for the aforesaid wrongful conduct and liable to the Plaintiff and the other members of the

Class for the substantial damages which they suffered in connection with their purchases of the Company's securities during the Class Period.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff prays for judgment as follows: declaring this action to be a proper class action; awarding damages, including interest; awarding reasonable costs, including attorneys' fees; and such equitable/injunctive relief as the Court may deem proper.

JURY DEMAND

Plaintiff demands a trial by jury.

Dated: February 26, 2008

KAPLAN FOX & KILSHEIMER LLP

By: ______________________
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-and-

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Attorneys for Plaintiff

CERTIFICATION OF NAMED PLAINTIFF
PURSUANT TO FEDERAL SECURITIES

I, Walter C. Schirmer, hereby certify and swear as follows:

1. I, Walter C. Schirmer, on behalf of the Minneapolis Firefighters' Relief Association ("MFRA"), have reviewed a Complaint against **Ambac Financial Group, Inc.** alleging violations of the securities laws and authorize its filing;

2. MFRA is willing to serve as a representative party on behalf of a class or to be a member of a group representing a class, including providing testimony at deposition and trial, if necessary;

3. MFRA has filed the following civil action as a representative party on behalf of a class in an action brought under the federal securities laws during the last three years:

   MFRA v. Bristol-Myers Squibb Company, et al., Case No. 07-cv-5867, U.S. District Court, Southern District of New York

4. The following is a description of MFRA's transactions during the class period specified in the Complaint in the securities of **Ambac Financial Group, Inc.**:

Security Name	Transaction Type	Trade Date	Shares	Price
Ambac Financial Group, Inc.	Purchase	03/16/2006	1,625	$80.7489
Ambac Financial Group, Inc.	Purchase	03/21/2006	871	$81.3480
Ambac Financial Group, Inc.	Purchase	11/01/2006	947	$83.5770
Ambac Financial Group, Inc.	Purchase	11/02/2006	475	$83.7120
Ambac Financial Group, Inc.	Sale	10/24/2007	1,158	$52.3967
Ambac Financial Group, Inc.	Sale	10/24/2007	305	$52.6900
Ambac Financial Group, Inc.	Sale	10/30/2007	685	$39.8911
Ambac Financial Group, Inc.	Sale	10/30/2007	517	$40.3400
Ambac Financial Group, Inc.	Sale	11/01/2007	1,253	$28.7652

5. MFRA did not purchase securities of **Ambac Financial Group, Inc.** at the direction of its counsel or in order to participate in any private action under the federal securities laws;

6. MFRA will not accept any payment for serving as a representative party on behalf of a class beyond its pro rata share of any recovery, except as ordered or approved by the Court.

I declare under penalty of perjury that the foregoing is true and correct.

Date: 2-25—, 2008

W.C. Schirmer

Walter C. Schirmer, Executive Secretary
Minneapolis Firefighters' Relief Association